

## Internal Revenue Service

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Person To Contact:

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CC:CORP:04

PLR-139756-06

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### Legend

Distributing =

Controlled =

Sub 1 =

Sub 2 =

Sub 3 =

Sub 4 =

Sub 5 =

LLC 1 =

LLC 2 =

LLC 3 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

a =

b =

c =

Business A =

Business B =

Business C =

Series X =

Series Y =

Dear \_\_\_\_\_ :

This letter responds to your August 18, 2006 letter requesting rulings on certain federal income tax consequences of a proposed transaction. The information provided in that letter and in later correspondence is summarized below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process. In particular, this office has not reviewed any information pertaining to, and has made no determination regarding, whether the proposed transaction: (i) satisfies the business purpose requirement of § 1.355-2(b) of the Income Tax Regulations; (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (see § 355 (a)(1)(B) of the Internal Revenue Code and § 1.355-2(d)); and (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or the controlled corporation (see § 355(e)(2)(A)(ii) and § 1.355-7).

### **Summary of Facts**

Distributing is a publicly traded holding company that is the common parent of an affiliated group of corporations filing a consolidated federal income tax return. As of Date 1, Distributing had outstanding a shares of common stock.

Distributing is indirectly engaged in Business A and Business B (collectively, the "Distributing Businesses") and Business C. Business A is primarily conducted by Sub 1 and Business B is primarily conducted by Sub 2. Sub 1 and Sub 2 are wholly owned subsidiaries of Distributing.

Distributing formed Controlled on Date 2 and contributed all of the stock of Sub 3 to Controlled on Date 3 in return for a single share of Controlled common stock, which represented all of the issued and outstanding shares of Controlled. Sub 3 was directly engaged in Business C. Immediately following the contribution, Sub 3 converted to a limited liability company, LLC 2, which is a disregarded entity for federal income tax purposes (the "Controlled Restructuring"). The Controlled Restructuring was treated as a reorganization pursuant to § 368(a)(1)(F).

On Date 4, Controlled purchased all of the outstanding stock of Sub 4 from unrelated parties. Controlled then caused Sub 4 to convert to a limited liability company, LLC 3, which was a disregarded entity for federal income tax purposes. LLC 3 then caused its wholly owned subsidiary, Sub 5, to convert to a limited liability company, LLC 1, which is a disregarded entity for federal income tax purposes. Following the conversions of Sub 4 and Sub 5 to LLC 3 and LLC 1, respectively, Controlled contributed all of its membership interests in LLC 2 to LLC 3, which in turn contributed all of the membership interests in LLC 2 to LLC 1. On Date 5, LLC 3 merged into Controlled in a transaction that was disregarded for federal income tax purposes.

Immediately prior to Date 6, Controlled executed a recapitalization, issuing new Controlled Series Y voting shares in exchange for 100% of its existing issued and outstanding share (the "Recapitalization"). On Date 6, Controlled issued a new class of Series X voting shares ("IPO shares") in an initial public offering ("IPO"). Based on the voting rights of the Series X shares, the IPO shares represent approximately b percent of the voting power of all outstanding stock of Controlled. Distributing has retained approximately c percent of the voting power of all outstanding stock of Controlled. The IPO was consummated in contemplation of the proposed transaction.

The taxpayer has submitted financial information indicating that each of Distributing Business A and Business B, and Controlled Business C, each have had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

Distributing has determined, for valid business reasons, to separate Business A and Business B on the one hand, from Business C on the other. Specifically, the separation is intended to improve both Distributing's and Controlled's financing structure, including their ability to effectively and efficiently raise substantial amounts of capital by (i) facilitating the IPO that closed on Date 6 and (ii) optimizing Distributing's and Controlled's independent capital structures. The separation will also enhance the success of Distributing's and Controlled's business by enabling Distributing and Controlled to resolve management, systemic, and other problems arising from Distributing's ownership of the different business segments within its affiliated group.

### **Proposed Transaction**

In order to accomplish the above stated business purposes, Distributing proposes to distribute 100% of the Controlled Series Y common stock pro rata to Distributing shareholders (the "Distribution"). Distributing will distribute cash in lieu of issuing a fractional share to any shareholder that would otherwise be entitled to receive a fractional share of Controlled Series Y common stock.

## **Representations**

The following representations have been made in connection with the Distribution:

(a) The Distribution is not part of a plan or series of related transactions (within the meaning of § 1.355-7) pursuant to which one or more persons will acquire, directly or indirectly, stock representing a 50-percent or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).

(b) The indebtedness owed by Controlled to Distributing after the Distribution, if any, will not constitute stock or securities.

(c) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.

(d) Sub 1 and Sub 2 will constitute members of the separate affiliated group of Distributing within the meaning of § 355(b)(3) at the time of the Distribution.

(e) The five years of financial information submitted on behalf of Sub 1 and Sub 2, is representative of each corporation's present operations, and, with regard to each, there have been no substantial operational changes since the date of the last financial statements submitted.

(f) Following the Distribution, Distributing and Controlled each will continue the active conduct of its business independently and with its separate employees.

(g) The five years of financial information submitted on behalf of LLC 2 or its predecessor is representative of LLC 2's present operation, and, with regard to LLC 2, there have been no substantial operational changes since the date of the last financial statements submitted.

(h) The Distribution of the stock of Controlled is primarily carried out for the corporate business purpose of improving Distributing's and Controlled's capital structure, including their ability to effectively and efficiently raise a significant amount of capital on more favorable terms, by: (i) facilitating Controlled's stock offering that closed on Date 6, and (ii) optimizing Distributing's and Controlled's independent capital structures. The Distribution will also enhance the success of Distributing's and Controlled's business by enabling Distributing and Controlled to resolve management, systemic, and other problems arising from Distributing's ownership of the different business segments within its affiliated group. The Distribution of the stock of Controlled is motivated, in whole or substantial part, by the primary corporate business purposes.

(i) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying the aggregation rules of § 355(d)(7)) will hold stock possessing 50-percent or more of the total combined voting power of all classes of Distributing stock entitled to vote, or 50-percent or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.

(j) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50-percent or more of the total combined voting power of all classes of Controlled stock entitled to vote, or 50-percent or more of the total value of shares of all classes of Controlled stock, that was either (i) acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution, or (ii) attributable to distributions on Distributing stock or securities that were acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(5)) ending on the date of the Distribution.

(k) Subsequent to the Distribution, it is anticipated that Distributing and Controlled will share a number of administrative services for a transitional period not to exceed 12 months. Other than (i) trade account indebtedness created in the ordinary course of business through continuing transactions at terms comparable to those which could be obtained in an arm's length transaction, (ii) any liabilities that may arise from the tax sharing agreement, and (iii) payables created for all transitional services negotiated at arm's length, no intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution.

(l) Immediately before the Distribution, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable intercompany transaction regulations (See Treas. Reg. §§ 1.1502-13 and 1.1502-14 as in effect before the publication of T.D. 8597, 1995-32 I.R.B. 6, and as currently in effect; Treas. Reg. § 1.1502-13 as published by T.D. 8597). Further, Distributing's excess loss account with respect to the stock of Controlled, if any, will be included in income before the Distribution (See Treas. Reg. § 1.1502-19).

(m) Payments made in connection with all continuing transactions after the Distribution, if any, between Distributing and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(n) Neither Distributing nor Controlled is an investment company as defined in § 368(a)(2)(F)(iii) and (iv).

(o) Distributing, Controlled, and the shareholders of Distributing will each pay their own expenses, if any, incurred in connection with the Distribution.

(p) The payment of cash in lieu of a fractional share of Controlled Series Y common stock is solely for the purpose of avoiding the expense and inconvenience to Controlled of issuing fractional shares and does not represent separately bargained-for consideration. The total cash consideration that will be paid in the Distribution to the Distributing shareholders instead of issuing fractional shares of Controlled Series Y common stock will not exceed one percent of the total consideration that will be issued in the Distribution. The fractional share interests of each shareholder will be aggregated, and no shareholder will receive cash in an amount equal to or greater than the value of one full share of Controlled Series Y common stock.

(q) The transaction is not used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both.

(r) There is no plan or intention by Distributing or Controlled to convert shares of Controlled Series Y common stock to shares of Controlled Series X common stock.

(s) The Controlled Restructuring qualified as a tax-free reorganization pursuant to § 368(a)(1)(F).

(t) The Recapitalization qualified as a tax-free reorganization pursuant to § 368(a)(1)(E).

### **Rulings**

Based solely on the information submitted and the representations made, we rule as follows on the Distribution:

(1) No gain or loss will be recognized by Distributing upon the pro rata distribution of the Controlled Series Y common stock to the Distributing shareholders (§ 355(c)).

(2) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) Distributing shareholders upon their receipt of the Controlled Series Y common stock pursuant to the Distribution (§ 355(a)).

(3) The aggregate basis of the Distributing common stock and the Controlled Series Y common stock in the hands of Distributing shareholders, including a fractional share interest, will be the same as the basis in the Distributing common stock held by the Distributing shareholders immediately prior to the Distribution, allocated in proportion to the fair market values of the Distributing and the Controlled Series Y common stock in accordance with Treas. Reg. § 1.358-2(a)(2) and § 358(a)(1) and (b)).

(4) The holding period of the Controlled Series Y common stock received by the Distributing shareholders, including a fractional share interest, will, in each instance, include the holding period of the Distributing common stock with respect to which the distribution of the Controlled Series Y common stock is made, provided that the Distributing common stock is held as a capital asset on the date of the Distribution (§ 1223(1)).

(5) A shareholder who receives cash in lieu of fractional shares of Controlled Series Y common stock will recognize gain or loss measured by the difference between the basis of the fractional share received, as determined in ruling (3) above, and the amount of cash received (§ 1001). Any gain or loss will be treated as capital gain or loss, provided that such fractional shares of stock are held as capital assets on the date of the Distribution.

(6) As provided in § 312(h), the earnings and profits of Distributing and Controlled will be adjusted in accordance with Treas. Reg. § 1.312-10(b)).

### **Caveats**

No opinion is expressed about the tax treatment of the proposed transaction described above under other provisions of the Code and regulations or the tax treatment of any condition existing at the time of, or effects resulting from, the proposed transaction that is not specifically covered by the above rulings. In particular, no opinion is expressed regarding: (i) whether the proposed transaction satisfies the business purpose requirement of § 1.355-2(b); (ii) whether the proposed transaction is used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both; (iii) whether the proposed transaction is part of a plan (or series of related transactions) under § 355(e)(2)(A)(ii); and (iv) the tax consequences of the Controlled Restructuring and the Recapitalization.

### **Procedural Statements**

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent. A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.



In accordance with the power of attorney on file in this office, a copy of this ruling letter will be sent to your authorized representatives.

Sincerely,

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Richard K. Passales  
Senior Counsel, Branch 4  
Office of Associate Chief Counsel (Corporate)

cc: